SUPREME COURT, U. S.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-1417

HUMANE SOCIETY OF AUSTIN AND TRAVIS COUNTY,

Petitioner

v.

THE AUSTIN NATIONAL BANK, EXECUTOR OF THE ESTATE OF MARY MAYFIELD GUTSCH, DECEASED, *et al*,

Respondents

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE UNITED STATES

April 6, 1976

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To the Honorable, the Chief Justice and Associates Justices of the Supreme Court of the United States:

THE HUMANE SOCIETY OF AUSTIN AND TRAVIS COUNTY, the petitioner herein, prays that a writ of certiorari issue to review the judgment of the Supreme Court of Texas entered in the above-entitled case on January 7, 1976.

OPINIONS BELOW

The opinion of the Texas Supreme Court is reported at 531 Southwestern Reporter 2nd Series 574 and is printed in Appendix A hereto, infra, page 13.

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JURISDICTION

The judgment of the Supreme Court of Texas (Appendix A, infra, page) was entered on December 10th, 1975. A timely petition for hearing was denied on January 7th, 1976. The jurisdiction of the Supreme Court is invoked pursuant to 28 USC Sec. 1257 (3).

QUESTIONS PRESENTED

1. Whether the Federal Statutes, Regulations and cases prohibiting self-dealing apply to a National Bank-Executor.

2. Whether such Federal Statutes, Regulations and cases prohibiting self-dealing can be circumvented by a strained application of the "awaiting investment" exception.

3. Whether funds held by a National Bank-Executor under direct orders of the Probate Court to invest them can be "funds awaiting investment" for a period of sixteen months.

STATUTE INVOLVED

This case involves Section 9.12 of 12 Code of Federal Regulations entitled Self-Dealing, which provides as follows:

> "Unless lawfully authorized by the instrument creating the relationship, or by court order or by local law, funds held by a national bank as fiduciary shall not be invested in stock or obligations of, or property acquired from the bank or its directors, officers, or employees, or individuals with whom there exists such a connection, or organizations in which there exists such an interest, as might affect the exercise of the best judgment of the bank in acquiring the property, or in stock or obligations of, or property acquired from, affiliates of the bank or their directors, officers, or employees."

STATEMENT OF THE CASE

This is a case in which the HUMANE SOCIETY OF AUSTIN AND TRAVIS COUNTY, as residuary beneficiary of the Mary Mayfield Gutsch Estate, sought to avoid or offset executor and attorney fees charged by the AUSTIN NATIONAL

BANK while acting the role of executor for the Gutsch Estate on the basis that a fiduciary should not be allowed to profit out of his trust. The respondent bank used money held in its fiduciary capacity of executor and loaned it to itself in the form of purchasing its own certificates of deposit bearing lower interest rates than those of other financial institutions in the area.

In the Court of Civil Appeals and the Supreme Court of Texas, the Respondent successfully argued the proposition that such an action was permissible under 12 USCA Sec. 92a which in part states "Funds deposited or held in trust by the bank awaiting investment shall be carried in a separate account and shall not be used by the bank in the conduct of its business unless it shall first set aside in the trust department United States bonds or other securities approved by the Comptroller of the Currency." Alsa relied upon was Section 9.10 of 12 Code of Federal Regulations which states in part "Funds held in a fiduciary capacity by a national bank awaiting investment or distribution shall not be held uninvested or undistributed any longer than is reasonable for the proper management of the account" and "funds held in trust by a national bank, including managing agency accounts, awaiting investments or distribution may, unless prohibited by the instrument creating the trust or by local law, be deposited in the commercial or savings or other department of the bank, provided that it shall first set aside under control of the trust department as collateral security . . ."

The Supreme Court of Texas after quoting with approval the following excerpt from *Magruder v. Drury*, 235 US 106 (1914) at page 119:

> "It is a well-settled rule that a trustee can make no profit out of his trust. The rule in such cases springs from his duty to protect the interests of the estate, and not to permit his personal interests to in any wise conflict with his duty in that respect. The intention is to provide against any possible selfish interest exercising an influence which can interfere with the faithful discharge of the duty which is owing in a fiduciary capacity."

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then ruled that the Respondents investing its own certificates of deposit bearing lower interest rates was not an investment but was simply a deposit awaiting investment or distribution. This was in error because the Probate Court had ordered the Executor to invest the funds and distribution did not occur until more than sixteen months after the Respondent's first purchase of its own Certificates of Deposit.

In its Motion for Rehearing the Petitioner urged the Supreme Court of Texas to reconsider its decision. The Petitioner argued that 12 C.F.R. Sec. 1.12 prohibits any self-dealing and specifically prohibits a national bank acting in a position of trust, from investing funds held, in stock or obligations of itself. The Petitioner also urged the Court to accept its theory that monies held as certificates of deposits are invested, that certificates of deposit are investments and obligations of the bank and are not simply deposits.

The Motion for Rehearing was denied and the Supreme Court of Texas reaffirmed its decision concluding that the bank's purchase with estate funds of its own obligations, certificates of deposit, was permissible within the meaning of 12 USCA Sec. 92a since the funds were "awaiting investment" and that the bank was authorized to invest the funds in its own certificates of deposit pending final determination of their proper dispersal. The opinion appears in Appendix A of the Petition.

REASONS FOR GRANTING THE WRIT

The Supreme Court of Texas has ruled contrary to the Federal law, i.e., Section 9.12 of 12 Code of Federal Regulations entitled "Self-Dealing," and contrary to the United States Supreme Court Case of *Magruder v. Drury*, 235 US 106 (1914).

The Supreme Court of Texas has misconstrued the Federal statutes, Regulations and cases in order to allow a national bank acting as executor of an estate to self-deal by purchasing its own obligations. The opinion attached to this Petition allows a national bank-executor to borrow money from itself at

rates determined by itself. The bank-executor acting as lender is permitted to loan funds to itself as bank-borrower under the justification that the funds are awaiting investment or distribution.

If the opinion of the Supreme Court of Texas is allowed to stand, the well established rule prohibiting a fiduciary from profiting in any way through using funds held in its fiduciary capacity will be significantly diluted.

Facts

The Estate was being administered by the Executor-Bank under direct supervision of the Probate Court. A will construction suit was filed which the Executor-Bank, and the Probate Court knew it would require approximately two years to complete.

When received by the Executor-Bank, the Estate contained large holdings of inadequately productive stocks. On application of Petitioner, the Probate Court ordered the Executor-Bank to sell the stocks and *ordered* it to *invest* the *proceeds* ($883,000.00) in any one of several conservative investments, "certificates of deposits in banks and savings and loan institutions; day-in, day-out savings accounts; commercial paper in prime-rated corporations; U.S. Treasury bills, bonds or notes due within two years; and U.S. agency securities due within two years." A copy of the Probate Court's order is printed in Appendix A.

Notwithstanding such Probate Court order and the Federal Statutes, Regulations and cases prohibiting self-dealing, and over the protest of Petitioner that better and higher interest rates were available, the Executor-Bank invested the entire cash funds by purchasing its own certificates of deposit, and continued to do so until distribution some sixteen months later.

Funds Were Not "Awaiting Investment or Distribution"

The attempted justifications of "awaiting investment" or "awaiting distribution" does not fit the facts of this case.

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All funds held by an executor are literally "awaiting distribution." If the statutes and regulations allowing banks to deposit funds had intended that broad definition, it would simply have said "all funds" of the estate may be deposited in the executor-bank. Obviously the statutes and regulations intended something less than "all funds," and the only reasonable interpretation is funds awaiting *immediate* distribution.

In this case, a will construction suit was in progress, all parties knew it would be a long period of time before distribution could be made, and it was in fact over sixteen months before distribution was in fact made.

"Awaiting investment" likewise does not fit this case. The "awaiting investment" provision of the statutes and regulations should most reasonably be interpreted to allow the bank to deposit funds in its commercial bank for short periods until suitable investments can be made.

But in this case, the Probate Court had *ordered* the Executor-Bank to *invest* the funds in any of the five investments mentioned, including certificates of deposit, but not of the Executor-Bank. In fact, the very purpose of the Probate Court order was to sell the inadequately yielding investments (stocks) and to *re-invest* the proceeds in order to obtain a higher yield.

To hold that this $883,000.00, which the Probate Court had ordered invested, was a deposit, "awaiting investment" for a period of sixteen months, not only strains any reasonable interpretation of the regulations, but is in direct opposition to Section 9.10 of 12 Code of Federal Regulations which states in part: "Funds held in a fiduciary capacity by a national bank awaiting investment or distribution shall not be held uninvested or undistributed any longer than is reasonable for the proper management of the account."

It is hard to understand how the Texas Court can cite *Slay v. Burnett Trust*, 187 SW2d 377 (1945), quote from *Magruder v. Drury*, 235 US 106 (1914), and then apparently approve a self-dealing situation.

The Court correctly held in part as follows:

> ". . . the executor of an estate is held to the same fiduciary standards in his administration of the estate as a trustee . . . As a trustee of the property of the estate, the executor is subject to the high fiduciary standards applicable to all trustees."

Thereafter the Court quotes from the *Magruder* case, *supra*, and the principle embodied in the United States Supreme Court case at 235 US 120 cannot be emphasized too strongly:

> "It is a well-settled rule that a trustee can make no profit out of his trust. The rule springs from his duty to protect the interests of the estate, and not to permit his personal interest to in any wise conflict with his duty in that respect. The intention is to provide against any possible selfish interest exercising an influence which can interfere with the faithful discharge of the duty which is owing in a fiduciary capacity."

In the very next sentence following the *Magruder* quote, *supra*, the Texas Supreme Court states (page 4 of the opinion):

> "By purchasing its own certificates of deposit with funds of the Gutsch Estate which it held in trust as executor, the Bank in effect borrowed the funds for its own use."

The Court said the bank is entitled to use this money and profit thereby because the federal and state banking laws permit such acts so long as the funds are "awaiting investment."

The Court relied on the regulation interpreting "awaiting investment" issued by the Comptroller of the Currency at 12 C.F.R. Sec. 9.10, pursuant to 12 USCA Sec. 92a. But that regulation specifically says the funds may be used by a national bank "unless prohibited by . . . local law . . ."

The common law in the State of Texas has time and again prohibited a trustee from using trust funds in his business to

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derive a profit therefrom. No distinction has previously been made on the basis that the funds were fully secured from loss. No distinction has previously been made because the trustee was a bank and "was not, we believe, (acting) in furtherance of its own self-interest." (Opinion, page 10)

Whether or not the bank was acting "in furtherance of its own self-interest" or whether or not it acted in good faith are not issues in this case. The heretofore strictly enforced rule against self-dealing is to eliminate the possibility of self-interest or bad faith by a fudiciary. *Margruder v. Drury, supra.*

The purchase by a bank-executor of its own certificate of deposit is specifically prohibited by Texas statutes. Article 7425b-14, V.A.T.S., provides in part:

> "A corporate trustee shall not purchase for a trust shares of its own stocks or its bonds, obligations, or other securities . . ."

Article 7425b-12, V.A.T.S., provides in part:

> "A trustee shall not buy or sell, either directly or indirectly, any property owned by or belonging to the trust estate, from or to itself or an affiliate . . ."

Section 352 of the Probate Code, V.A.T.S., provides in part:

> "The personal representative of an estate shall not become the purchaser, directly or indirectly, of any property of the estate sold by him, or by any co-representative if one be acting."

These statutes absolutely prohibit the purchase by the bank-executor of its own certificates of deposit. Federal regulations also prohibit funds held by a fiduciary from being invested in itself or its obligations. 12 C.F.R. Sec. 9.12.

Sec. 9.12 Self-Dealing

(a) "Unless lawfully authorized by the instrument creating the relationship, or by court order or by local law, funds held by a national bank as fiduciary shall not be in-

vested in stock or obligations of, or property acquired from the bank or its directors, officers, or employees, or individuals with whom there exists such a connection, or organizations in which there exists such an interest, as might affect the exercise of the best judgment of the bank in acquiring the property, or in stock or obligations of, or property acquired from, affiliates of the bank or their directors, officers, or employees."

The Supreme Court of Texas through its interpretation of Section 9.12 along with Sections 9.10 or 12 Code of Federal Regulations and Section 92a of 12 USCA whittles at the general rule with the "awaiting investment" exception. The Texas opinion would permit a national bank-executor to invest trust funds or estate funds in its own obligations under the justification that the funds are "awaiting investment or distribution" and that the funds "should not be held uninvested or undistributed" for an unreasonable period of time.

The Petitioner would urge that a more proper interpretation of the statutes and regulations would prohibit the fiduciary from investment of funds in itself at any time, but would permit the "deposit" of the funds in itself if secured by United States bonds or other securities approved by the Comptroller of the Currency. Even in such instance, the deposit would be only for short periods of time if in fact the funds are awaiting investment or awaiting distribution.

A distinction should be made between funds invested in a fiduciary's own obligations and funds simply deposited or held by the fiduciary. Investing funds in a fiduciary's own obligations is self-dealing and specifically prohibited by Section 9.12 of 12 C.F.R. whereas funds deposited in or held by the fiduciary are permitted so long as the funds in actuality are awaiting investment or distribution.

In this case the funds were invested in the fiduciary's own obligations which constitutes self-dealing. The Respondent further strains credulity by proposing that certificates of deposit were not investments or obligations but were simply deposits and thus qualify for the exception.

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The Supreme Court of Texas improperly interpreted the application of the Federal statutes and regulations in its holding on pages 7 and 8 of its decision that, since these were funds "awaiting investment," the bank was thereby authorized to invest the funds in its own certificates of deposit pending final determination of their proper dispersal. Nowhere in any of the Federal Statutes or regulations is a fiduciary permitted to invest in itself or its own obligations.

In *Meinhard v. Salmon*, 249 N.Y. 458, 164 N.E. 545, 62 A.L.R. 1 (1928) Justice Cardoza expressed the strict legal prohibitions against self-dealing by a fiduciary:

> "Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctillio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions. • • • Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this court."

In *Johnson v. Peckham*, 132 Tex. 148, 120 SW2d 786, 120 A.L.R. 720 (1938), the late Justice Hickman speaking for our Supreme Court quoted approvingly from Justice Cardozo's *Meinhard* opinion and pronounced the rule governing fiduciary relationships in this State:

> "When persons enter into fiduciary relations each consents, as a matter of law, to have his conduct towards the other measured by the standards of the finer loyalties exacted by courts of equity. That is a sound rule and *should not be whittled down by exceptions.*"

In Bogert, *Trusts and Trustees*, 2d Ed Sec. 543(j), p. 548, it is stated:

"The trustee may violate the duty of loyalty by *lending trust funds to himself*. He thus brings into play a conflict of private and representative interests. As lender it is his duty to get the best terms possible as to interest, security, and maturity. As debtor his impulse is naturally in the direction of getting the money at the lowest rate and often on other terms not advantageous to the lender."

The prohibition against self-dealing by a fiduciary, heretofore one of the most revered rules of our American jurisprudence, should not under any circumstances be "whittled down" by exceptions such as have been approved by the Texas Supreme Court in this case. We urge this Court to enforce the prohibition against self-dealing and to deny profit to anyone in violation thereof.

CONCLUSION

For the foregoing reasons Petitioner prays that a writ of certiorari be granted.

Respectfully submitted,

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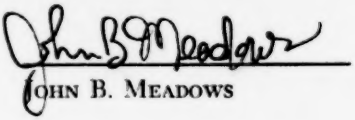
CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing Petition for Writ of Certiorari has been mailed, certified mail, to Mr. James P. Hart and Mr. James H. Keahey, 904 Brown Building, Austin, Texas, attorneys for respondent, this 6th day of April, 1976.



JOHN B. MEADOWS

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APPENDIX A

OPINION BELOW

IN THE SUPREME COURT OF TEXAS

No. B-5044

HUMANE SOCIETY OF AUSTIN AND TRAVIS COUNTY, Petitioner	I	
v.	I	From Travis County
THE AUSTIN NATIONAL BANK, EXECUTOR OF THE ESTATE OF MARY MAYFIELD GUTSCH, DECEASED ET AL, Respondent	I	Ninth District

This is a case in which petitioner, the Humane Society of Austin and Travis County, is challenging commissions and attorneys' fees claimed by Austin National Bank as dependent executor of the estate of Mary Mayfield Gutsch, deceased. The probate court allowed the claims as submitted and disallowed all offsets claimed by the Humane Society, and the Court of Civil Appeals affirmed. 517 S.W.2d 323.

By its first three points of error the Humane Society contends that the Bank was guilty of self-dealing in investing the estate's funds in its own certificates of deposit pending distribution of those funds. In points four and five the Humane Society contends that the Bank incurred unnecessary expenses for maintenance and storage of property in the estate. In point six the Humane Society contends that the Bank is not entitled to claim attorneys' fees incurred in a prior suit seeking a construction of decedent's will because the work performed by the attorneys was of no benefit to the estate. We overrule all points of error and affirm the judgment of the Court of Civil Appeals.

Mary Mayfield Gutsch died on October 19, 1971, in Travis County, Texas, leaving a holographic will in which Austin

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National Bank was named executor. The will was probated in Travis County on November 1, 1971, and the Bank qualified as dependent executor. The Bank instituted suit seeking a declaratory judgment to determine the rights of the named beneficiaries under the will. The outcome of that suit was finally determined by this Court in our decision of December 13, 1973, City of Austin v. Austin National Bank, 503 S.W.2d 759. As it was finally construed, the will devised to a god-child all tangible personal property found in Mrs. Gutsch's house at her death; the house and the land upon which it was located was devised to the City of Austin to be used as a public park; and the remainder of the estate (approximately two-thirds) was devised to the Humane Society in fee.

On September 11, 1972, the Bank made an application to the probate court, joined by the Humane Society, to sell certain bank and other stock of the estate and re-invest the funds in other securities yielding a better return, pending the outcome of the will construction suit. On September 15, 1972, the probate court entered an order authorizing such sale and listing the types of securities in which the Bank could re-invest the proceeds, including certificates of deposit in banks and savings and loan institutions. Pursuant to this order the Bank sold the estate's stock and, in September and November of 1972, purchased certificates of deposit from its own commercial department with the proceeds. These certificates, in the total amount of $883,000.00, were renewed from time to time over the succeeding sixteen months.

The Humane Society contends that under the common law of trusts and the provisions of the Texas Trust Act, the Texas Banking Code, and the regulations of the Federal Comptroller

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of Currency, the Bank was absolutely prohibited from investing funds of the estate with itself. For this alleged breach of the Bank's fiduciary duty the Humane Society seeks to deny the bank its commission as executor and to recover any profits made by the bank from use of the money invested in the certificates of deposit.

First, it is clear that the Texas Trust Act, TEX. REV. CIV. STAT. ANN. articles 7425b-1 through 7425b-47, is not applicable here. Article 7425b-2 states that a "trust" for purposes of the Act "means an express trust only, . . ." In City of Austin v. Austin National Bank, supra, we held that Mrs. Gutsch's will did not create a perpetual charitable trust, but vested the residuary estate in the Humane Society in fee. Even though the estate's funds were held by the Bank in a fiduciary capacity for the benefit of the Humane Society as beneficiary of the estate, the duties of the Bank arose by reason of its position as executor of the estate, not as trustee of any express trust created by the will. An express devise of property to another as trustee for named beneficiaries is required for creation of an express trust. Fitz-Gerald v. Hall, 150 Tex. 39, 237 S.W.2d 256 (1951). Moreover, the trustee of an express trust is given authority, absent limiting provisions in the instrument creating the trust, to exchange and invest property of the trust, article 7425b-25; a dependent executor of an estate has no such power absent an authorization from the probate court or an express grant of authority from testator. TEX. PROB. CODE ANN. § 234 (supp. 1974).

Even though the Texas Trust Act is not applicable, the executor of an estate is held to the same fiduciary standards in his administration of the estate as a trustee. Section 37 of

the Probate Code provides, in part, that the executor "shall recover possession of and hold such estate in trust to be disposed of in accordance with law." As trustee of the property of the estate, the executor is subject to the high fiduciary standards applicable to all trustees. In Slay v. Burnett Trust, 143 Tex. 621, 187 S.W.2d 377 (1945), this Court quoted with approval the following excerpt from Magruder v. Drury, 235 U.S. 106 (1914), at page 119:

> It is a well-settled rule that a trustee can make no profit out of his trust. The rule in such cases springs from his duty to protect the interests of the estate, and not to permit his personal interest to in any wise conflict with his duty in that respect. The intention is to provide against any possible selfish interest exercising an influence which can interfere with the faithful discharge of the duty which is owing in a fiduciary capacity.

By purchasing its own certificates of deposit with funds of the Gutsch estate which it held in trust as executor, the Bank in effect borrowed the funds for its own use. Austin National Bank contends that it was expressly authorized to invest the estate's funds in its own certificates of deposit by the provisions of 12 U.S.C.A § 92a (supp. 1975), and TEX. REV. CIV. STAT. ANN. art. 342-604 (1973). 12 U.S.C.A. § 92a provides that the Comptroller of the Currency shall be authorized to grant to national banks the power to act as executor of estates to the same extent that state banks are permitted such power. The statute requires national banks to segregate all assets held in a fiduciary capacity, and provides that

> . . . funds deposited or held in trust by the bank awaiting investment shall be carried in a separate account and shall not be used by the bank in the conduct of its business unless it shall first set aside in the trust department United States bonds or other securities approved by the Comptroller of the Currency.
>
> 12 U.S.C.A. § 92a(d).

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The Comptroller of the Currency has issued regulations pursuant to section 92a granting to national banks power to act as executor coextensive with the authority of state banks. 12 C.F.R. Chapter I, Part 9. Thus federal law allows a national bank to deposit trust funds with itself when such funds are "awaiting investment," provided that (1) it sets aside in its trust department approved securities equal in face value to the amount of the fund, and (2) local law authorizes such a deposit.

Article 342-604 of the Texas Banking Code provides:

> Unless the trust instrument provides otherwise, funds received in trust by a state bank awaiting investment shall be carried in a separate account and shall not be used by the bank in the conduct of its business, unless it shall first set aside in the trust department United States government bonds or other securities eligible under the laws of this State for the investment of funds by guardians or trustees of a market value equivalent to the amount so used . . . .

"[F]unds received in trust" within the meaning of this statute includes funds received by a bank as executor. Under these state and federal statutes, a bank may temporarily deposit with itself funds of an estate "awaiting investment" provided it sets aside adequate security. It is undisputed that Austin National Bank complied with the security requirement by setting aside in its trust department qualified securities equal in value to the certificates of deposit. The question to be decided, therefore, is whether the funds used to purchase the certificates of deposit were "awaiting investment" within the meaning of Article 342-604 and the corresponding federal law.

The Comptroller of the Currency has issued the following regulation, at 12 C.F.R. § 9.10, pursuant to 12 U.S.C.A. § 92a:

> § 9.10. Funds Awaiting Investment or Distribution
>
> (a) Funds held in a fiduciary capacity by a national bank awaiting investment or distribution shall not be held uninvested or undistributed any longer than is reasonable for the proper management of the account.

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(b) Funds held in trust by a national bank, including managing agency accounts, awaiting investment or distribution may, unless prohibited by the instrument creating the trust or by local law, be deposited in the commercial or savings or other department of the bank: Provided, that it shall first set aside under control of the trust department as collateral security:

(1) Direct obligations of the United States, or other obligations fully guaranteed by the United States as to principal and interest; or

(2) Readily marketable securities of the classes in which state banks exercising fiduciary powers are authorized or permitted to invest trust funds under the laws of the state in which such national bank is located; or

(3) Other readily marketable securities that qualify as investment securities pursuant to the Investment Securities Regulation of the Comptroller of the Currency, 12 C.F.R., Chapter I, Part 1. The securities so deposited or securities substituted therefor as collateral shall at all times be at least equal in face value to the amount of trust funds so deposited, but such security shall not be required to the extent that the funds so deposited are insured by the Federal Deposit Insurance Corporation. The requirements of this section are met when qualifying assets of the bank are pledged to secure a deposit in compliance with local law, and no duplicate pledge shall be required in such case.

It is apparent from this regulation that the Comptroller has interpreted the term "awaiting investment" in § 92a to mean "awaiting investment or distribution." The Comptroller's broad interpretation of § 92a comports with the interpretation of Article 342-604 urged by the Bank in this case.

In American Legion Post No. 90 of Village of Mamaroneck v. First National Bank and Trust Co. of Mamaroneck, 113 F.2d 868 (2nd Cir. 1940), the Court construed the term "awaiting investment" in the statute from which § 92a was derived, 12 U.S.C.A. § 248(k). In that case some investors had placed proceeds from the sale of land with the bank pending their distribution to the investors. Because of litigation concerning the proper allocation of taxes arising from the sale,

the proceeds remained in the bank's trust department for several years, during which time the bank paid three percent interest on the funds. The bank had set aside securities to secure the trust fund as required by § 248(k) and the corresponding regulations. When the bank became insolvent the investors attempted to claim their lien on the securities so set aside, and the general creditors of the bank challenged the lien, contending that the funds were not "awaiting investment" within the meaning of § 248(k). The Court agreed with the investors, stating, at page 872:

> Perhaps more serious is the further claim that these were not funds held in trust "awaiting investment" and hence without the statute. We think, however, that this is too narrow a construction of the statute, and really defeats its intent. If trust funds held for investment are subject to the statute, but trust funds held for distribution are only general assets of the bank, then we find a serious difference in result following from a very slight, even formalistic, change in the relations of the parties. It would be no great stretch to term this a fund held "for investment," particularly since the desire of the subscribers for some increment on their funds was made so clear. . . .
>
> Moreover, a broader interpretation should be given to the statute. We think that the provisions for security include in general the fiduciary funds which the bank is required to keep segregated from its general assets.

We agree with the construction placed upon § 92a by the Court of Appeals for the Second Circuit and by the Comptroller, and we believe that the same interpretation should be placed upon article 342-604 of the Banking Code. The Gutsch estate's funds were held by the Bank in its fiduciary capacity as executor of the estate, and the Bank was required to keep the funds segregated from its general assets. The Bank held the funds temporarily, pending the outcome of litigation which would determine whether it would place them in a charitable trust or distribute them to the beneficiaries. We hold that these

were funds "awaiting investment" within the meaning of article 342-604 and 12 U.S.C.A. §92a, and that the Bank was thereby authorized to invest the funds in its own certificates of deposit pending final determination of their proper dispersal. This interpretation most fully effectuates the purpose of the statute to allow efficient temporary investment of funds held in trust by a bank pending their ultimate disposition, while providing maximum security for those funds.

The Humane Society next contends that, even if the Bank's purchase of its own certificates of deposit was not wrongful per se, the Bank should be liable for profits which it could have realized by investing the funds in certificates of other banks and savings and loan institutions. The Humane Society offered proof at trial that the higher interest rates offered by other banks would have yielded $3,775.66 more over the sixteen months during which the funds were invested.

Although article 342-604 and 12 U.S.C.A. § 92a authorize the Bank to use the trust funds in the conduct of its business provided it sets aside the proper security, these statutes do not relieve the Bank of its fiduciary duty to the estate. The Bank holds the estate funds in trust for the beneficiaries, and in its dealings with the fund the Bank must act in scrupulous good faith, casting aside completely its personal interest and opportunities for gain resulting from the fiduciary relationship. See Johnson v. Peckham, 132 Tex. 148, 120 S.W.2d 786 (1938); TEX. PROB. CODE ANN. § 230(a) (1956). Austin National Bank's conduct in carrying out the probate court's order to sell the estate's bank stock and re-invest the proceeds must be measured by these strict fiduciary standards.

The order of the probate court authorized the Bank to invest the estate's funds in:

> . . . certificates of deposit in banks and savings and loan institutions; day-in, day-out

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savings accounts; commercial paper in prime-rated corporations; U. S. Treasury bills, bonds or notes due within two years; and U. S. agency securities due within two years.

Mr. George K. Meriwether, senior vice-president and trust officer of the Bank, who was in charge of the administration of the Gutsch estate, testified that at the time the estate's bank stock was sold the interest rates for day-in, day-out savings accounts, U. S. Treasury bills, bonds and notes due within two years, and U. S. agency securities due within two years were less than interest rates offered by Austin National Bank on its certificates of deposit. He testified that he believed the interest rates for commercial paper in prime-rated corporations were lower than the Bank's rates also. This testimony was not challenged by the Humane Society. Another officer of the Bank testified that the interest rates paid on certificates of deposit purchased with estate funds were always at least equivalent to or more than the Bank's "published rates," the rates offered general customers of the Bank. This testimony is uncontradicted. Mr. Meriwether also testified that the Bank allowed him to cash in some certificates of the estate before their maturity dates and purchase new certificates at higher rates when it was advantageous to do so, and that other banks in the area would not have allowed him to do so.

The Humane Society offered evidence that other banks and savings and loan institutions in the Austin area were offering interest rates as much as one percent higher than rates offered by Austin National Bank on comparable certificates of deposit during the seventeen-month period that the estate's funds were invested in Austin National Bank's certificates. Based on this evidence, the Humane Society contends that by investing in these other institutions' securities the estate funds could have earned $3,775.66 more in interest during these seventeen months. While the Bank contests this figure, its officers admitted that other institutions were offering higher interest

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rates on certificates of deposit, and that the funds would have returned a better profit if invested in certificates of other institutions.

The rate of return, however, is not the only criterion for determining the propriety of the Bank's investment decision in this case. The safety of the trust fund is also a primary consideration of the fiduciary. Republic National Bank & Trust Co. v. Bruce, 130 Tex. 136, 105 S.W.2d 882 (Tex. Comm. App. 1937, opinion adopted). This is especially true of funds of an estate held by an executor, whose primary duty is preservation of the estate for distribution. Austin National Bank set aside in its trust department qualified securities equivalent in value to the certificates of deposit purchased with the estate's funds, as required by the regulations of the Comptroller. Mr. Meriwether testified that other banks and institutions were prohibited by law from providing security for their certificates of deposit issued to general customers over the $20,000.00 limit set by the Federal Deposit Insurance Corporation and state law. This testimony, which was not challenged or contradicted, indicates that the Bank could not have obtained one hundred percent security by investing the estate's funds in certificates of deposit of any other financial institution. The total interest earned on the Austin National Bank certificates of deposit during the sixteen-month period was $85,815.11, the interest rates varying from six to ten percent. Thus the extra interest of $3,775.66 to which the Humane Society contends it is entitled constitutes less than five percent of the total interest paid. The Bank's decision to forego this extra income and obtain instead the full security offered by its own certificates of deposit was not, we believe, in furtherance of its own self-interest to the detriment of the estate.

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The Bank was investing the estate's funds in short-term certificates of deposit in order to be in a position to make prompt distribution of the money upon final conclusion of the court proceedings in the will construction case. From the time of the first investment in the certificates of deposit to the time the funds were delivered to the Humane Society was slightly less than sixteen months. During all of this time the estate was in litigation. The bank officers testified that they intentionally made short-term investments so they could be ready to deliver the estate on short notice. The distribution promptly occurred as soon as the litigation ceased.

Under the circumstances of this case the Bank did not breach its fiduciary duty as executor by preferring its own certificates of deposit over those of other institutions. The portion of the offset seeking $3,775.66 in lost income was properly denied by the probate court.

The Humane Society also seeks offsets against the Bank's claims for $8,731.13, the cost of taking care of the house and land given to the City of Austin and the storage fee for furniture and other personal property given to Mrs. Gutsch's godchild. The Bank had the duty to take care of the estate's assets as a prudent man would take care of his own property. TEX. PROB. CODE ANN. § 230(a) (1956). This duty continued until the suit seeking a construction of the will was finally disposed of. These offsets were properly denied by the probate court.

Finally, the Humane Society challenges the Bank's claim for $8,100.00 in attorneys' fees and legal expenses for representation of the estate through the appeal of the will construction suit, on the ground that the representation was only for the benefit of the Bank and not the estate. We do not agree. There were serious questions concerning the

construction of the will. The Bank's duty as executor was to determine the testatrix's intent and distribute the estate in accordance therewith; the actions of the Bank were in good faith and in accord with its duty to the estate. There is no contention that the amount of the claim for attorneys' fees is not reasonable. The Bank's claim was properly allowed. Rowe v. Dyess, 213 S.W. 234 (Tex. Comm. App. 1919).

The judgment of the Court of Civil Appeals is affirmed.

Ross E. Doughty
Justice

Chief Justice Greenhill not sitting.

Opinion delivered December 10, 1975.

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APPENDIX B

STATUTES AND REGULATIONS INVOLVED

12 CFR Section 9.12 Self-Dealing.

(a) Unless lawfully authorized by the instrument creating the relationship, or by court order or by local law, funds held by a national bank as fiduciary shall not be invested in stock or obligations of, or property acquired from, the bank or its directors, officers or employees, or individuals with whom there exists such a connection, or organizations in which there exists such an interest, as might affect the exercise of the best judgment of the bank in acquiring the property, or in stock or obligations of, or property acquired from, affiliates of the bank or their directors, officers or employees.

12 CFR Section 9.10 Funds awaiting investment or distribution.

(a) Funds held in a fiduciary capacity by a national bank awaiting investment or distribution shall not be held uninvested or undistributed any longer than is reasonable for the proper management of the account.

(b) Funds held in trust by a national bank, including managing agency accounts, awaiting investment or distribution may, unless prohibited by the instrument creating the trust or by local law be deposited in the commercial or savings or other department of the bank, provided that it shall first set aside under control of the trust department as collateral security:

(1) Direct obligations of the United States, or other obligations fully guaranteed by the United States as to principal and interest; or

(2) Readily marketable securities of the classes in which state banks exercising fiduciary powers are authorized or permitted to invest trust funds under the laws of the state in which such national bank is located; or

(3) Other readily marketable securities that qualify as investment securities pursuant to the Investment Securities Regulation of the Comptroller of the Currency, 12 CFR, Chapter I, Part 1.

The securities so deposited or securities substituted therefor as collateral shall at all times be at least equal in face value to the amount of trust funds so deposited, but such security shall not be required to the extent that the funds so deposited are insured by the Federal Deposit Insurance Corporation. The requirements of this section are met when qualifying assets of the bank are pledged to secure a deposit in compliance with local law, and no duplicate pledge shall be required in such case.

12 USCA Section 92a. Trust Powers - Authority of the Comptroller of the Currency.

(a) The Comptroller of the Currency shall be authorized and empowered to grant by special permit to national banks applying therefor, when not in contravention of State or local law, the right to act as trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, committee of estates of lunatics, or in any other fiduciary capacity in which State banks, trust companies, or other corporations which come into competition with national banks are permitted to act under the laws of the State in which the national bank is located.

(b) Whenever the laws of such State authorize or permit the exercise of any or all of the foregoing powers by State banks, trust companies, or other corporations which compete with national banks shall not be deemed to be in contravention of State or local law within the meaning of this section.

(c) National banks exercising any or all of the powers enumerating

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in this section shall segregate all assets held in any fiduciary capacity from the general assets of the bank and shall keep a separate set of books and records showing in proper detail all transactions engaged in under authority of this section. The State banking authorities may have access to reports of examination made by the Comptroller of the Currency insofar as such reports relate to the trust department of such bank, but nothing in this section shall be construed as authorizing the State banking authorities to examine the books, records, and assets of such bank.

(d) No national bank shall receive in its trust department deposits of current funds subject to check or the deposit of checks, drafts, bills of exchange, or other items for collection or exchange purposes. Funds deposited or held in trust by the bank awaiting investment shall be carried in a separate account and shall not be used by the bank in the conduct of its business unless it shall first set aside in the trust department United States bonds or other securities approved by the Comptroller of the Currency.

(e) In the event of the failure of such bank the owners of the funds held in trust for investment shall have a lien on the bonds or other securities to set apart in addition to their claim against the estate of the bank.

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APPENDIX C

NO. 33,700.

ESTATE OF MARY MAYFIELD	)	IN THE COUNTY COURT OF
	)	
GUESCH, DECEASED	)	TRAVIS COUNTY, TEXAS.

ORDER FOR SALE OF
COMMON STOCKS AND REINVESTMENT

On this 15th day of September, 1972, came on to be heard the application for sale of common stocks and reinvestment by the Austin National Bank, executor of this estate, joined by The Humane Society of Austin and Travis County, the principal beneficiary by trust or otherwise of the personal property of this estate, filed herein on September 11, 1972. Having considered such application and being of the opinion that it should be granted, it is therefore

ORDERED that the executor be and it is hereby authorized to sell at public auction or privately, for cash, the following common stocks owned by this estate:

(1) 969 shares of stock in The Austin National Bank, Austin, Texas, at not less than $57.00 per share.

(2) 4,444 shares of Merchants and Planters Bank of Sherman, Texas, stock at not less than $75.00 per share.

(3) ~~6,200~~ 6,116 shares of The First National Bank in Dallas stock at not less than $32.00 per share.

(4) 750 shares of Security Financial Services, Inc., Sheboygan, Wisconsin, stock at not less than $49.00 per share

It is further ORDERED that the executor be and it is hereby authorized to purchase with the proceeds of such sale, certificates of deposit in banks and savings and loan institutions; day-in, day-out savings accounts; commercial paper in prime-rated corporations; U. S. Treasury bills, bonds or notes due within two years; and

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U. S. agency securities due within two years.

Signed, rendered, and entered this 15th day of September, 1971.

/s/

J. E. WATSON
COUNTY JUDGE, TRAVIS COUNTY, TEXAS.

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MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-1417

HUMANE SOCIETY OF AUSTIN AND TRAVIS COUNTY,
Petitioner,

v.

THE AUSTIN NATIONAL BANK, EXECUTOR OF THE ESTATE OF MARY MAYFIELD GUTSCH, DECEASED, ET AL.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF TEXAS

BRIEF OF RESPONDENTS IN OPPOSITION

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April 15, 1976.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-1417

HUMANE SOCIETY OF AUSTIN AND TRAVIS COUNTY,
Petitioner,

v.

THE AUSTIN NATIONAL BANK, EXECUTOR OF THE ESTATE OF MARY MAYFIELD GUTSCH, DECEASED, ET AL.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF TEXAS

BRIEF OF RESPONDENTS IN OPPOSITION

To The Honorable Supreme Court Of The United States:

The Respondents, The Austin National Bank, Executor of the Estate of Mary Mayfield Gutsch, Deceased, and the firm of Hart, Keahey, & Hart, Respondents, respectfully submit this opposition to the petition for a writ of certiorari to review the judgment of the Supreme Court of Texas.

OPINIONS BELOW

The opinion of the Texas Supreme Court is reported in *Humane Society of Austin and Travis County, Petitioner* v. *The Austin National Bank, Executor of the Estate of*

Mary Mayfield Gutsch, Deceased, et al., Respondents, 531 S.W.2d 574. The opinion of the Texas Court of Civil Appeals, which was affirmed by the Texas Supreme Court, is reported in *Humane Society of Austin and Travis County, Appellant* v. *Austin National Bank, Executor of Estate of Mary M. Gutsch, Deceased, Appellee,* 517 S.W.2d 323.

JURISDICTION

Petitioner asserts jurisdiction under the provisions of 28 U.S.C. § 1257(3). Apparently Petitioner's claim of jurisdiction is that it has asserted, and has been denied, a right under a federal statute, 28 U.S.C. § 92a, which is not referred to in the petition under the heading "Statute Involved" but which is copied in the later part of Appendix B to the petition, relating to the authority of the Comptroller of the Currency to authorize national banks to exercise certain powers as fiduciaries, including the powers of executor, and to regulate the exercise of such powers. Two of the regulations which have been promulgated by the Comptroller of the Currency are 12 C.F.R. Section 9.12, relating generally to the subject of "Self-Dealing", and 12 C.F.R. Section 9.10, relating to "Funds Awaiting Investment or Distribution." The Petitioner apparently contends that the first of these regulations is applicable. All of the lower courts held that the second regulation, 12 C.F.R. § 9.10, was the applicable regulation and that the Respondent Bank properly acted under the provisions of this regulation.

QUESTION PRESENTED

There is really only one question in this case, which is whether the Texas Supreme Court properly held that 28 U.S.C. § 92a, and the Comptroller's Regulation, 12 C.F.R. § 9.10, legally justified the action of the Respondent Bank pending the outcome of the case involving the construc-

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tion of the Decedent's will, in purchasing certificates of deposit in its own commercial bank, on which it paid its regular "published rates" of interest, and which deposits were secured 100% by securities approved by the Comptroller of the Currency.

STATUTE INVOLVED

Under the heading of "Statute Involved" Petitioner does not cite any statute but refers to a regulation of the Comptroller of the Currency, 12 C.F.R. § 9.12, which relates to the general subject of "Self Dealing" by national banks. As we have stated above, in fact the statute involved is 28 U.S.C. § 92a, paragraphs (a)-(e) copied in the second half of Appendix B, attached to the petition for certiorari. While the regulation regarding "self-dealing", 12 C.F.R. § 9.12 applies as a general rule to national banks, it clearly does not apply to the specific situation covered by the other regulation of the Comptroller of Currency relating to "funds awaiting investment or distribution", 12 C.F.R. § 9.10.

STATEMENT OF THE CASE

The statement of the case in the petition for certiorari is, we submit, inadequate and the following brief summary is necessary to an understanding of the case and the issues involved.

The decedent, Mary Mayfield Gutsch, died in Austin, Texas, on October 19, 1971, leaving a holographic will (copied in the opinion of the Texas Supreme Court construing the will, *City of Austin* v. *The Austin National Bank*, 503 S.W.2d 759, at 760), in which she undertook to dispose of an estate appraised at more than $1,600,000.00 to the City of Austin, eight individuals, the Petitioner the Humane Society of Austin and Travis County, and another charity, Goodwill Industries.

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Near the beginning of her will, Mrs. Gutsch said, "I want the Austin National Bank to administer my estate". The Bank offered the will for probate and the County Court of Travis County by order dated November 1, 1971, probated the will and appointed the Bank dependent executor, which meant under the Texas law that generally speaking the Bank as executor had to apply for and secure the approval of the Court for all that it did, the will not providing for an independent executorship under the Texas law.

As Mrs. Gutsch wrote her will, she left many questions regarding the disposition of her estate which required a judicial construction of the will. The Bank, in its capacity as executor, filed a will construction suit in the District Court of Travis County, Texas, making all of the beneficiaries defendants and also, as required by Texas statute, making the Attorney General of Texas a defendant, because some of the beneficiaries were charities.

There were numerous questions involving the rights as between the named beneficiaries to parts of Mrs. Gutsch's estate. Since all of the beneficiaries were represented by their own attorneys and the Attorney General was authorized to protect the interests of the charities, the Bank took no active position in any of the controversies between the beneficiaries. However, there was one issue between the Bank and the Humane Society in which the Bank alone had standing to present what it considered to be the proper construction of Mrs. Gutsch's will. That question was whether the will created a perpetual charitable trust of all of the income from the residue of the estate (approximately ⅔ of the estate property) or whether it made a gift outright of the entire residue to the Humane Society. The will provided that "all of the income from the remainder of my estate shall go to the Humane Society" but it made no provision regarding the principal of the remainder. If

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under the law, the will created a charitable trust, the duty of the Bank as executor was to hold the principal of the remainder and pay only the income to the Humane Society. On the other hand, if the will should be construed to be an outright gift of the remainder to the Humane Society, then the duty of the Bank was to deliver to the Humane Society the principal as well as all income from the residue.

The Bank took the position that a charitable trust was created; the Humane Society took the position that the will made an outright gift of the remainder to the Humane Society.

The judgment of the trial court, dated March 8, 1972, held that a charitable trust was created. This holding was affirmed by the Court of Civil Appeals in *The City of Austin* v. *The Austin National Bank,* 488 S.W.2d 586 (Tex. Civ. App., Aus., 1972), but the Supreme Court of Texas reversed the judgments of the lower courts and held that an outright gift of the remainder to the Humane Society was intended by Mrs. Gutsch's will. *City of Austin* v. *The Austin National Bank,* 503 S.W.2d 759 (Tex. Sup., 1973, rehearing den'd, 1/16/74). The Bank as executor, then distributed the part of the residue it still held to the Humane Society. A total amount of principal and interest of about $1,500,000.00, has been distributed to the Humane Society.

During the time that the Bank had been acting as executor and performing the duties which were required of it by the Texas law, including the gathering together of all of the assets, the preparation and filing of an inventory, the payment of claims, the preparation and filing of tax returns, the safeguarding of the property, the keeping of records, the filing of reports, securing necessary orders, and the distribution of the parts of the property bequeathed

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or devised to various beneficiaries, the Bank collected no commissions for its services. On February 15, 1974, the Bank filed its claim for a total commission of $40,000.00, reciting that the statutory commission permitted by the Texas statutes would have been substantially more. There is no question in this case but that the amount of the commission was within the law and reasonable for the services rendered. The sole question is whether the Bank should be required, in effect, to forfeit its commission to the Humane Society because of its action, pending the final determination of the will construction case, in using part of the estate's funds to purchase certificates of deposit in its commercial bank. (The Humane Society also claimed that the Bank's attorneys were not entitled to fees to be paid from estate funds for their services on the appeal of the will construction case, but since this question involves purely a question of state law, it will not be discussed in this brief.).

The County Court allowed the Bank's claim for commissions in the amount it asked, and the action of the County Court in allowing these commissions has been upheld by the Texas appellate courts. *Humane Society of Austin and Travis County* v. *Austin National Bank, Executor of the Estate of Mary M. Gutsch, Deceased,* 517 S.W.2d 323 (Tex. Civ. App. Beaumont, 1974), and *Humane Society of Austin and Travis County* v. *The Austin National Bank, Executor,* 531 S.W.2d 574 (Tex. Sup., 1975).

ARGUMENT

1. The Decision Below Is Clearly Correct.

The proper decision of this case, in so far as it involves any federal question, depends on the proper construction

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of the first five paragraphs of 12 U.S.C. § 92a, paragraphs (a)-(e), and the construction by the Comptroller of the Currency of these statutory provisions in the regulations he promulgated relating to funds held in a fiduciary capacity, awaiting investment or distribution, contained in 12 C.F.R. § 9.10. A brief historical outline of the background of this statute (which is officially Pub. L. 87-222, § 1, September 28, 1962, 78 Stat. 668) and of the Regulation referred to should be given for a proper understanding of the case.

Before the enactment of the 1962 Act referred to above, the authority to grant permits to National Banks to act in fiduciary capacities was vested in the Board of Governors in the Federal Reserve System by the Federal Reserve Act, § 11 (k), 12 U.S.C. § 248 (k), which contains substantially the same provisions as are now found in 12 U.S.C. 92 (a), paragraphs (a)-(e). Under the authority of this statute, the Board of Governors of the Federal Reserve System had issued their Regulation F which interpreted the words funds held in trust "awaiting investment" to include funds received and held in trust "awaiting investment or distribution." While this statute and this regulation were in effect, the question of the proper construction of the statute and the regulation came up in the case of *American Legion Post No. 90 of Village of Mamaroneck* v. *First National Bank and Trust Company of Mamaroneck*, 113 F.2d 868 (Second Cir., 1940). The facts in that case were that funds had been placed with the Bank and Trust Company which had been raised for the purpose of the erection of a community house as a memorial for the veterans for the First World War. The Bank treated the funds as trust funds and carried them in its trust department and set aside securities for the protection of the funds as provided in the statutes and the regulation

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of the Board of Governors of the Federal Reserve System then in effect. Interest at the rate of 3% per annum was paid on these funds. Later the Bank and its successor bank became insolvent, and the question was whether the beneficiaries of the trust fund were entitled to a lien on the securities which had been set aside in conformity with the regulation of the Board of Governors of the Federal Reserve System. The parties claiming that the lien should not be enforced asserted that the regulation exceeded the authority granted in the statute regarding funds "awaiting investment" so as to include "funds awaiting investment or distribution.". The Court of Appeals, in an opinion written by Judge Charles E. Clark, held that the regulation was authorized by the statute and that the Bank had properly placed the trust funds in its commercial bank in a time deposit, and had properly set aside securities for the protection of the fund. We quote the relevant parts of the Court's opinion (113 F.2d at 872-873):

> "Perhaps more serious is the further claim that these were not funds held in trust 'awaiting investment,' and hence without the statute. We think, however, that this is too narrow a construction of the statute, and really defeats its intent. If trust funds held for investment are subject to the statute, but trust funds held for distribution are only general assets of the bank, then we find a serious difference in result following from a very slight, even formalistic, change in the relations of the parties. It would be no great stretch to term this a fund held "for investment', particularly since the desire of the subscribers for some increment on their funds was made so clear. It was not to be fully paid in for a year and a half; it was to bear interest at a substantial rate, it was subject to various difficulties of adjustment, including income tax litigation and other litigation which remained unsettled on the bank's failure more than four years after the first receipts were had.

> Moreover, a broader interpretation should be given to the statute. We think that the provisions for security include in general the fiduciary funds which the bank is required to keep segregated from its general assets. Such, indeed, is the view taken by the Board of Governors of the Federal Reserve System in their Regulation F promulgated under the power to issue regulations granted by this same statute. This regulation provides that when funds received and held in the trust department if a national bank 'awaiting investment or distribution' are deposited in the commercial or savings department of the bank to the credit of the trust department, security for the deposit must be provided in the shape of United States bonds or other specified assets of the bank."
>
> ". . .
>
> "With respect to a regulation required by the statute for the carrying into effect of its terms, we should not hesitate to take judicial notice so far as is necessary. The point is not decisive here, since all we are saying is that the interpretation made by the Board of Governors of the Federal Reserve System accords with our own. It also accords with the conclusions reached in the other cases cited. Carcaba v. McNair, supra; Fesenmeyer v. Ticonic Nat. Bank, 307 U.S. 161, 59 S.Ct. 777, 83 L.Ed. 1184."

The decision of the Court of Appeals in this case was not appealed to the Supreme Court. We submit that it is reasonable to assume that the reason there was no appeal or attempt to take the case to the Supreme Court by a petition for writ of certiorari was that the decision was clearly right. As the Court well knows, Judge Charles E. Clark, the author of the opinion in the *Mamaroneck* case, was recognized as an extremely able judge. See for example, Memorial Proceedings in his honor in the preface to 328 F.2d, pps. 5-23 (1964).

So far as we have been able to discover, no case has questioned the conclusion reached by the Court in the Mamaroneck case. The only two other cases discussing the statute (12 U.S.C. § 248 (k)) were Alabama cases, *First National Bank* v. *Weaver*, 225 Ala. 160, 142 So. 420, 88 A.L.R. 201 (1932), and *First National Bank* v. *Basham*, 238 Ala. 500, 191 So. 873, 125 A.L.R. 656 (1939). These cases held that the deposit of funds by the National Banks in their trust departments, pending distribution, was authorized by 28 U.S.C. § 248 (k) and further went on to hold that a similar rule would be applied to Alabama state banks. In the Alabama cases, it was held that the Bank was not even liable for interest, having complied with the regulation by depositing securities for the trust funds. In the first case, 88 A.L.R. at 205, the Court said that "we are of the opinion that under the facts herein disclosed, there appears to be no self-dealing or advantage or profit within the condemnation of the rule of decisions", and in the second case, 125 A.L.R. at 662, the Court said that "as a business proposition, such deposits may enable the trustee to do a good service to the trust estates at less expense" and that the transactions in question should be upheld because they were "in the common interest of the trustee and the trust estates in his keeping."

It may be also noted that in the decision of the Supreme Court of Texas which is involved in this case (Petition, Appendix A, p. A-5) the Court quotes Article 342-604 of the Texas Banking Code which provides in substance for the deposit of trust funds by a State Bank awaiting investment, provided securities are set aside by the Bank to insure the repayment of the trust funds. The Supreme Court (Petition, Appendix A, p. A-7) agrees with the construction of the Federal statute in the *Mamaroneck* case and holds that as a matter of state law the same construction of the Texas Banking Code should be adopted.

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The control of National Banks was changed from the Board of Governors of the Federal Reserve System to the Comptroller of the Currency in 1962 by Pub. L. 87-222, and is now codified as 12 U.S.C. § 92a. The United States Senate Report on the 1962 Bill is found in 1962 U.S. Code Cong. & Adm. News, p. 2735. The report refers to the existing statute, 12 U.S.C. § 148 (k) and says that the 1962 Act will make no change in the substative provisions of the existing law other than to transfer the authority from the Board of Governors of the Federal Reserve System to the Comptroller of the Currency, "so that there is no alteration of existing law regarding national banks in fiduciary capacities."

The Senate report makes no reference to the decision in the *Mamaroneck* case, which had been decided twenty-two years earlier, but we submit, that it is only reasonable to assume that the Congress was aware of the construction of the statute which had been given in the *Mamaroneck* case, and the fact that no alteration was made in the existing law regarding the actions of national banks in fiduciary capacities is, we submit, a proper basis for the inference that the Congress was satisfied with the construction in the *Mamaroneck* case.

Returning to the specific facts in this case, which are not in dispute, the statement made in the petition for certiorari is incomplete and likely to give the wrong impression regarding the action of the Respondent Bank in this case. We therefore add the following summary.

At the time of her death, Mrs. Gutsch owned substantial blocks of stock in the First National Bank of Dallas and the Merchants and Planters Bank of Sherman, Texas. During the pendency of the will construction suit, the Humane Society as beneficiary of all of the income on the residue,

was being paid by the Bank periodically. However, the Humane Society desired to have a greater income than was being produced by the dividends on the bank stocks referred to. The Respondent Bank had no authority to sell any of the estate under the provisions of the will and under Texas law could not make any such sale without a court order. Furthermore, the Respondent Bank was of the opinion that the stock in the Dallas and Sherman Banks had a potential for growth in the value of the principal which might well outweigh any increased income that might result from a sale of the stocks and the purchase of other securities. However, the Humane Society insisted upon the sale of these bank stocks. Before it would ask the Court for authority to make the sale, the Respondent Bank insisted that the Board of Directors of the Humane Society adopt a resolution requesting the Bank to sell the stocks at not less than stated prices and agreeing to indemnify the Respondent Bank and hold it harmless against any loss that might result if, in fact, the bank stocks should increase in value more than the increase in income which would result from their sale and the purchase of other securities yielding a higher rate of income. The Board of Directors of the Humane Society adopted this resolution, and therefore the Bank, joined by the Humane Society, applied for an order of sale, which included the stocks of the banks in Dallas and Sherman. The result was the order which is copied as Appendix C in the petition for certiorari, dated September 15, 1972.

The impression which the petitioner apparently wants the Court to have from its statement for the sale of these stocks is that the Respondent Bank was forced to make this sale by the order of the County Court. The facts are that the Respondent Bank applied for and obtained the order of the Court, in an effort to comply with the wishes of the Humane Society.

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The Court will note that the order of the Probate Court provided that the Respondent Bank was authorized to purchase with the proceeds of the sale designated securities, including "certificates of deposits in banks". There is nothing in the order that requires the Respondent Bank to use the proceeds to purchase certificates of deposit in *other* banks. The decision of the Respondent Bank was to purchase certificates of deposits in its own commercial department, secured, as required by the applicable federal statute and the regulation of the Comptroller of the Currency, by approved securities equal to the full value of the trust funds with which the certificates of deposit were purchased.

The principal reason which motivated the bank in purchasing certificates of deposit in its own commercial department was that such certificates of deposit would be 100% insured by the deposit of approved securities. It is settled law in Texas that "the safety of the trust funds is the first care of the law, and on this depends every rule which has been made for the conduct of trustees." See *Republic National Bank and Trust Company* v. *Bruce*, 130 Tex. 136, 105 S.W.2d 882, 884 (1937). The Texas law is, so far as we know, universally followed in other jurisdictions, as shown, for example, in 76 Am. Jur. 2d "Trusts" § 375, pps. 588-589 (1975), where it is stated that in handling funds in a fiduciary capacity, "safety is always a prime consideration" and that safety is "the first and income the second consideration."

The Respondent Bank used $550,000 of the proceeds of the sale of the Dallas and Sherman bank stocks in purchasing certificates of deposit beginning on September 28, 1972. It used an additional $330,000 of these proceeds in purchasing other certificates of deposit beginning on November 16, 1972. Beginning January 14, 1974, it combined

the certificates of deposit in one certificate for $883,000.00, bearing 9% interest. In every instance the Respondent Bank paid at least the "published" rate, or, in other words, the regular rate that it paid to its regular customers on certificates of deposit in like amounts.

No other Bank could have secured the deposits by setting aside securities, as the Austin National Bank was authorized to do in the present case. See for example, *Texas and Pacific Railway Co.* v. *Pottorf,* 63 F.2d 1 (5th Cir. 1933), in which the Court held that while the Bank was authorized to give security for money which is borrowed from others, it had no authority, generally, to pledge its assets for deposits. The exceptional situation involved in this case, and permitted by 28 U.S.C. § 92a and the regulations of the Comptroller of the Currency, 12 C.F.R. § 9.10 would not of course, apply to banks other than Respondent Bank, which other banks were not holding the funds of the Gutsch estate in a fiduciary capacity.

Moreover, by depositing the funds in its own commercial bank, the Respondent Bank was able to mature certificates of deposit early and replace them with other certificates in equal amounts bearing higher rates of interest, which was an important advantage during the period in question when rates of interest were fluctuating widely. No other bank would allow the early maturity and the issuance of other certificates of deposit bearing higher rates of interest.

For all of the reasons stated above, it is submitted that the Austin National Bank acted properly in depositing the proceeds of sales of the Dallas and Sherman Bank stocks in certificates of deposit in its own commercial bank. In fact, it is submitted that the Respondent Bank would have been delinquent in its duties had it failed to give proper

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consideration to the primary requirement that funds held in their fiduciary capacity should be so used that there is no danger of any loss of the fiduciary funds.

Petitioner asserts that other institutions were paying higher rates of interest than those paid by the Respondent Bank on the certificates of deposit. However, testimony to this effect related to certificates of comparable size which, however, were unsecured, except by the $20,000 insurance provided by the Federal Deposit Insurance Corporation or the Federal Savings and Loan Insurance Corporation in effect at that time. It is submitted that as a matter of common knowledge investments which are 100% secured generally bring a somewhat lower rate of interest than unsecured investments.

However, we do not want the Court to get the impression that the Respondent Bank paid any lower rate of interest on the certificates of deposit purchased with the funds of the Gutsch Estate than it paid at the same time to its regular customers on similar certificates of deposit which could not be secured because they were not funds held by the Bank in a fiduciary capacity and therefore did not come under the statute and the Comptroller's regulation involved in this case. The undisputed testimony is that the bank paid at least as much interest on the Gutsch estate certficates of deposit, even though they were fully secured, as it paid on unsecured certificates of deposit to its regular customers, and on occasions paid slightly more than the "published rates".

The Petitioner also asserts that Respondent Bank made a "profit" out of the purchase of its own certificates of deposit. There was no evidence that the Bank in fact realized from the use of these funds more than it paid on the certificates of deposit, particularly when it is borne in

mind that the Bank set aside, as it was required to do, securities at least equal in value to the amounts of the certificates of deposit. The setting aside of these securities prevented the bank from using them to secure other deposits, such as deposits of public funds. The important consideration, however, is that these certificates of deposit were 100% secured, which security could not have been obtained in any other bank or in any savings institution.

The argument in the petition that the Respondent Bank was making "investments" and not "deposits" when it purchased certificates of deposit in its own commercial bank, is of course without substance. Certificates of deposit are simply one kind of a deposit. See for example 10 Am.Jur.2d "Banks" § 45, p. 426 and *Michie on Banks and Banking*, 1973, Volume 5B, § 313, pps. 235-236, where it is said:

> "The basic principles which govern other type of bank deposits are applicable to certificates of deposit."

We frankly are at a loss to understand exactly what the Petitioner means by the second paragraph from the bottom of page 9 of the petition. Apparently the Petitioner argues that it would be all right to make a demand deposit of the estate's funds with its commercial bank, but that it was improper for the Respondent Bank as executor to purchase certificates of deposit which brought the Humane Society an income according to the terms of the certificates of deposit. Of course both demand deposits and certificates of deposit represent obligations on the part of the Bank to repay money that has been deposited with it. If anything, it seems clear to us that the distinction which should be made should be in favor of certificates of deposit paying an income to the Humane Society as contrasted with demand deposits which would simply require the Bank to

repay the principal amount of the deposit without paying any income or interest.

Petitioner makes a play on words regarding "investments". Of course the bank stocks of the Dallas and Sherman banks were themselves investments, made by Mrs. Gutsch and her deceased husband, which were held by the decedent at the time of her death. The sale of these investments by the Bank and the purchase of certificates of deposit were "reinvestments" of the proceeds of such sale. Obviously, however, what the statute and the Comptroller's regulation contemplated when they said funds "awaiting investment" was funds awaiting *permanent* investment. Where the proper disposition of the funds could not properly be determined until the conclusion of the will construction case, then it is submitted that, within the meaning of the statute, the funds were properly designated as funds "awaiting investment". If the Supreme Court had held that a perpetual charitable trust had been created, then the Bank as trustee, would be authorized to make *permanent* investments, taking into account the security of such investments and the income that they would yield for the benefit of the Humane Society. On the other hand, as long as there was a possibility (which turned out to be the case) that the will would be construed to make an outright gift to the Humane Society of all of the residue, the Bank could not make any permanent investments, but had to hold the funds in the form of short term securities, which could be readily cashed and a distribution made to the Humane Society when the questions of proper distribution were settled. Therefore, the order provides that the executor is "authorized to purchase with the proceeds of such sale" designated short term securities, with the evident purpose that such securities could be liquidated when the will construction case finally decided when the Bank should make *permanent* investments of the funds as trust

funds, or should distribute the entire residue including principal as well as income, to the Humane Society so that it could do whatever it pleased with the cash and securities which were distributed to it by the Respondent Bank. Our purpose in pointing out this fact to the Court is not to make a play upon words with the term "investment", but simply to point out that, even though the purchase of any kind of securities could in a sense be regarded as an "investment", the type of securities that could be purchased under the Probate Court's order were not the kind of *permanent* investments which the statute and the regulation evidently intended to refer to when it spoke of funds "awaiting investment".

Petitioner also argues that, in substance, the provision in the regulation of the Comptroller of the Currency regarding funds "awaiting distribution" is in effect meaningless, since all estate funds are awaiting distribution. It is of course true that, except for the parts of the estate that are required to pay debts, costs, taxes, and other proper expenses, the funds of an estate generally are awaiting distribution according to the provisions in the will. However, of course this would not be true of the principal funds which are to be held in trust in perpetuity for a charitable corporation since, in that event, only the income is often distributable. The question was unsettled whether there was, under the provisions of Mrs. Gutsch's will, a perpetual charitable trust for the benefit of the Humane Society, which would receive all of the income from the "remainder" or residue of the estate, or whether all of the residue, including the principal as well as any accrued income therefrom, should be paid to the Humane Society.

This is obviously a case to which the statute and the regulations of the Comptroller were intended to apply. The Respondent Bank of course was under an obligation

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not to pay the funds to any person who was not entitled to receive them. It could not validly distribute the principal residue of the estate to the Humane Society unless and until the Supreme Court of Texas held that Mrs. Gutsch's will did not create a perpetual charitable trust, but instead made an outright gift of the residue to the Humane Society. Promptly after this decision became final, the distribution was made by the Respondent Bank. Neither the statute nor the regulation gives any authority to a bank as fiduciary to hold trust funds such as funds of the estate, after it is clear that the funds should be distributed and in what manner and to whom. As soon as these questions were determined, the residue of the estate was distributed. Plainly until that time, the funds were "awaiting distribution" within the meaning of the Comptroller's regulation.

2. There Is No Conflict Of Decisions.

The only federal case cited in the petition which, it is claimed, conflicts with the decision of the Supreme Court of Texas in this case is *Magruder* v. *Drury*, 235 U.S. 106 (1914). That case in no way involved the statute and the regulation of the Comptroller which authorized the deposits made by the Respondent Bank in the present case. It was simply a case where one of several individual trustees made a profit by using trust funds to purchase notes from a firm of which he was a member and which charged commissions on notes which were so purchased by trust funds. The opinion in the *Magruder* case states general rules regarding the duties of fiduciaries, which have simply no application to the actions of the Respondent Bank, which under *specific* statutory and regulatory authority.

Petitioner also cites two Texas cases, *Slay* v. *Burnett Trust*, 143 Tex. 621, 187 S.W.2d 377 (1945) and *Johnson* v. *Peckham*, 132 Tex. 148, 120 S.W.2d 86, 120 A.L.R. 720 (1938); a New York case, *Meinhardt* v. *Salmon*, 249 N.Y.

458, 164 N.E. 545, 62 A.L.R. 1 (1928); and a text, *Bogert "Trusts and Trustees"* 2d Ed. Sec. 543 (j) p. 48, as being in conflict with the decision of the Supreme Court of Texas in the present case. Even if this were so, there would not be the kind of conflict which would authorize the granting of a writ of certiorari in the present case. However, an examination of these cases and of the texts shows that the cases involved entirely different situations, showing fiduciary misconduct and not actions authorized by any statute or regulation, as in this case; and that the text is speaking of the general situation, and not of the specific situation involved in this case. The Supreme Court of Texas in this case recognized the wisdom of the general rules, but it also recognized that in the particular facts in this case, the Respondent Bank had not been guilty of any fiduciary misconduct and, in fact, had acted properly and in the best interests of the Humane Society.

While the Petitioner cites inapplicable sections of the Texas Trust Act, dealing with other situations, we respectfully call the Court's attention to the part of the Texas Trust Act which deals with the situation comparable to that in the present case. In 1943, the Texas Legislature adopted, as a part of the Texas Trust Act, Article 7425b-11, which reads as follows:

> "Art. 7425b-11. Corporate trustee depositing trust funds with self.
>
> A corporate trustee may deposit with itself trust funds which are being held pending investment, distribution, or to pay debts, provided it maintains under control of its trust department (if it has a trust department separate from its banking department) as security for such deposit a separate fund consisting of securities legal for trust investments which have at

all times during the deposit a total market value equal to the amount of the deposit. No such security shall be required to the extent said deposit is insured or otherwise secured by or under state or federal law. The separate fund of securities shall be marked as such. Withdrawals from or additions to it may be made from time to time, as long as the required value is maintained. The income of such securities shall belong to the corporate trustee."

We quote the above statute because we think that it is only fair to the Supreme Court of Texas to make it plain that it was not going against the Texas law regarding fiduciaries in the present case but, on the contrary, was following the policy established by the Texas Legislature in the particular situation we have in the present case, which accords with the policy established by the Congress regarding national banks.

CONCLUSION

For the foregoing reasons, Respondents respectfully pray that the writ of certiorari be denied.

April 5, 1976.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that three printed copies of the foregoing opposition to the Petition for Writ of Certiorari have been mailed, first class postage prepaid, to Mr. John B. Meadows, Counsel of Record for Petitioner, at his office address, 313 East Anderson Lane, Suite 310, Austin, Texas 78752, April 15, 1976.

James P. Hart

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